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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1950.

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No.

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CHENERY CORPORATION, ET AL., *Petitioners,*

v.

SECURITIES AND EXCHANGE COMMISSION, ET AL.

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## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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Petitioners pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit, entered in the above-entitled case on April 2, 1951.

### OPINIONS BELOW

The opinion and order of the Commission (R. 7-32) and its supplemental opinion and order (R. 34-42) are reported as Holding Company Act Release No. 8318 and No. 8387, respectively. The memorandum opinion of the District Court (R. 52-58) is reported in 87 F. Supp. 289. The opinion of the Court of Appeals (R. 317-326) is not yet reported.

## JURISDICTION

The judgment of the Court of Appeals was entered on April 2, 1951 (R. 327). The jurisdiction of this Court is invoked under U. S. Code, Title 28, Section 1254 (1).

## QUESTION PRESENTED

Whether the court below has given proper effect to the decisions of this Court in the first and second *Chenery* cases in requiring petitioners, upon the basis of those decisions, to accept a plan of liquidation, despite the fact that the District Court concluded that there is no substantial evidence to support the Commission's findings that the liquidation plan is fair and equitable to petitioners.

## STATUTES INVOLVED

Sections 11(e) and 18(f) of the Public Utility Holding Company Act of 1935, 49 Stat. 822, 832, U. S. Code, Title 15, Secs. 79k(e) and 79r(f) provide:

> Sec. 11(e) "In accordance with such rules and regulations or order as the Commission may deem necessary or appropriate in the public interest or for the protection of investors or consumers, any registered holding company or any subsidiary company of a registered holding company may, at any time after January 1, 1936, submit a plan to the Commission for the divestment of control, securities, or other assets, or for other action by such company or any subsidiary company thereof for the purpose of enabling such company or any subsidiary company thereof to comply with the provisions of subsection (b). If, after notice and opportunity for hearing, the Commission shall find such plan, as submitted or as modified, necessary to effectuate the provisions of subsection (b) and fair and equitable to the persons affected by such

plan, the Commission shall make an order approving such plan; and the Commission, at the request of the company, may apply to a court, in accordance with the provisions of subsection (f) of section 79r of this chapter, to enforce and carry out the terms and provisions of such plan. If, upon any such application, the court, after notice and opportunity for hearing, shall approve such plan as fair and equitable and as appropriate to effectuate the provisions of this section, the court as a court of equity may, to such extent as it deems necessary for the purpose of carrying out the terms and provisions of such plan, take exclusive jurisdiction and possession of the company or companies and the assets thereof, wherever located; and the court shall have jurisdiction to appoint a trustee, and the court may constitute and appoint the Commission as sole trustee, to hold or administer, under the direction of the court and in accordance with the plan theretofore approved by the court and the Commission, the assets so possessed.

Sec. 18(f) "Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this chapter, or of any rule, regulation, or order thereunder, it may in its discretion bring an action in the proper district court of the United States, the district court of the United States for the District of Columbia, or the United States courts of any Territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices and to enforce compliance with this chapter or any rule, regulation, or order thereunder, and upon a proper showing a permanent or temporary injunction or decree or restraining order shall be granted without bond. The Commission may transmit such evidence as may be available concerning such acts or practices to the

Attorney General, who, in his discretion, may institute the appropriate criminal proceedings under this chapter."

## STATEMENT

Much of the history of this controversy is stated in the opinions of the Court in *Securities and Exchange Commission* v. *Chenery Corp.*, 318 U. S. 80 (the first *Chenery* case), and *Securities and Exchange Commission* v. *Chenery Corp.*, 332 U. S. 194 (the second *Chenery* case).

On November 8, 1937, Federal Water Service Corporation registered with the Commission as a holding company and filed with the Commission a plan of voluntary reorganization under the Public Utility Holding Company Act (R. 59). Amended plans were filed thereafter, and discussions were had with the staff of the Commission, and in March 1940 a new plan of reorganization was filed proposing a merger of Federal Water Service Corporation and two of its subsidiaries, Utility Operators Company and Federal Water and Gas Corporation (R. 59-60).

During this period, from November 8, 1937, to June 30, 1940, petitioners purchased preferred stock in Federal Water Service Corporation, in varying amounts as set forth at R. 60. Petitioners were at that time officers and directors of either Federal Water Service Corporation or Utility Operators Company; the Chenery Corporation, also a petitioner, was and is a corporation controlled by petitioner C. T. Chenery (R. 60-61).

The District Court specifically found that these purchases were for valid purposes, and that "there was no double dealing, fraud or lack of disclosure in making the purchases" (R. 61). This finding is not challenged by the court below.

All such purchases stopped abruptly when, on June 29, 1940, the Commission issued tentative findings on the merger plan in which the Commission for the first time, raised a question whether such purchases were proper, and whether the preferred stock thus purchased by petitioners should be allowed to participate equally with other preferred stock in the proposed merger (R. 61). Later, on March 24, 1941, the Commission held that petitioners could not be permitted to participate *pari passu,* because they had breached a fiduciary duty to the other stockholders (R. 61; 117-125). Shortly thereafter the Commission approved, over petitioners' objections, an amended plan which restricted petitioners to cost of stock plus 4 percent interest to the date of the merger, which was required by the plan to be prior to November 1, 1941. (R. 61; 117-125). The merger agreement was then submitted to the stockholders, approved by a requisite majority and became effective on October 30, 1941 (R. 61). Petitioners voted the stock acquired by them against the merger, and announced their intention to seek to have the limitations upon them set aside (R. 62).[1]

The proceeding which petitioners immediately instituted resulted in a decision by this Court that the

[1] Petitioners had, in fact, already filed a petition to review the order of the Commission in the Court of Appeals for the District of Columbia (R. 126). Their letters to the Board of Directors of Federal with their proxies against the merger so stated, and continued that "if, in the proceeding taken * * * to review the order" it should be affirmed, they would surrender their stock, and if it was modified or set aside, they would accept stock *pari passu* instead of demanding its value in cash (R. 62). That proceeding finally resulted in the order being set aside, by the mandate of the Court of Appeals upon the decision and mandate of this Court (318 U. S. 80). However, when Federal took the steps necessary to permit petitioners to accept the stock, the Commission refused to permit the arrangement to be carried out.

Commission's order of September 24, 1941, could not be sustained. *Securities and Exchange Commission* v. *Chenery Corporation,* 318 U. S. 80. The Court found that the general equitable precedents invoked by the Commission in support of its action did not justify it in denying petitioners parity with the other preferred shareholders, and remanded the case to the Commission.

Shortly thereafter, Federal filed with the Commission a request for approval of an amendment to the merger plan to permit petitioners parity treatment (R. 62). Almost two years later, with no further evidence, the Commission refused its approval (R. 63; 131-173). The Commission this time asserted that although petitioners' claims could not be restricted on the grounds of general equitable principles, they could and should be by the special and peculiar circumstances arising from the nature of the Commission's functions under the Act and the voluntary reorganization process established by that Act (R. 150). This Court, upon review, refused to disturb what it called "an allowable judgment" and declined to hold that the Commission was "forbidden from utilizing this particular proceeding for announcing and applying a new standard of conduct". *Securities and Exchange Commission* v. *Chenery Corporation,* 332 U. S. 194, 203 (1947).

Meanwhile, on December 31, 1942, Federal had filed with the Commission a plan under Section 11 of the Act looking toward its ultimate dissolution or merger with another company (R. 66). Parts of this plan, and certain supplemental plans, were approved by orders of the Commission beginning in 1943 (*e.g.,* 12 S.E.C. 766). On November 7, 1947, Federal submitted to the Commission an amended and supplemental plan, pur-

suant to Section 11 (e) of the Act, proposing its own liquidation and dissolution and providing for the satisfaction of all claims against it and distribution of its remaining assets to its stockholders. The plan provided for alternate methods for distributing its assets among its shareholders dependent upon the Commission's determination as to what limitations should be put upon the claims of petitioners (R. 66, 9).

The Commission set down Federal's plan for hearing and specified as one of the issues: the amount of Federal's assets that should be set aside in satisfaction of the claims of the petitioners in order to effectuate the purposes of Section 11(b) of the Act and to make the plan fair and equitable to the persons affected by it (R. 5-6). The petitioners sought leave to intervene to oppose an inequitable limitation of their claims, and were heard (R. 70). After hearing, the Commission approved Federal's plan of dissolution on condition that it be amended to provide that $313,190 be set aside in full and complete satisfaction of petitioners' claims (R. 7-32). The Commission held, first, that the Merger Plan, which both it and this Court had previously considered, constituted a final determination that payment of $313,190 in full satisfaction of petitioners' claims would be fair and equitable (R. 18). The Commission went on, however, to consider independently what amount the petitioners might be allowed in the dissolution of Federal, and decided that it would not be fair and equitable to allow them anything in excess of $313,190, the cost of their preferred stock plus interest at 4 percent to October 31, 1941, the effective date of the merger (R. 20-22). A plan amended to conform to the Commission's opinion was approved on July 27, 1948 (R. 34).

The Commission applied to the District Court of Delaware, pursuant to Section 11(e) and 18(f) of the Act, to enforce the plan of Federal as amended in accordance with its order (R. 3). In its application for enforcement the Commission requested, *inter alia*, that the District Court issue an appropriate order enforcing the provisions of the plan as approved by the Commission and enjoining all claimants against Federal, including the petitioners, from taking any action that might tend to interfere with the carrying out of the provisions of the plan (R. 4.). Except for Section 3 of the plan, which provided that payment to petitioners of $313,190, representing the cost of their stock plus interest to October 1, 1941, would be in full satisfaction of petitioners' claims, the plan was promptly, and without opposition, ordered enforced (R. 1).

The District Court was clear as to the merits of Section 3 of the plan, relating to petitioners' claims. It rejected the Commission's independent determination as to its fairness and equity, and stated that it would have

> "no hesitation in holding there is no substantial evidence to support the Commission's finding that Chenery should be penalized and limited to cost plus interest for its preferred stock purchases" (R. 57)

The District Court also stated that

> "Chenery successfully shows that the policy of the Commission—to prohibit and penalize purchases of stock by officers and directors during reorganization—was only an avowed policy in that it was never followed by the Commission, except in the instant case; and if such policy ever existed it was clearly abandoned by the Commission six

> months prior to the time it entered the order now on review in the instant case." (R. 56)

Nevertheless, the Court stated that it was compelled to approve and enforce Section 3, as requested by the Commission, because of the decision of this Court in the second *Chenery* case, 332 U. S. 194.

Petitioners appealed to the Court of Appeals for the Third Circuit (R. 69), but prior to the consideration of the appeal by that court sought, without success, a writ of certiorari from this Court, 340 U. S. 831. Thereafter, on April 2, 1951, the court below affirmed the judgment of the District Court (R. 327). The opinion below states that the rights of petitioners have been "conclusively determined in the prior reorganization and merger proceedings" (R. 322). The court did not indicate any disagreement with the conclusion of the District Court that the "rule" penalizing stock purchases by management pending reorganization had been abandoned immediately after penalizing petitioners herein, but stated that the argument of petitioners that they should not be the victims of a "rule" applied only in their case, "while it has its appeal, is not available to defeat the operation of the rule of res judicata" (R. 325).

## SPECIFICATION OF ERRORS TO BE URGED

1. In holding that petitioners' rights were conclusively determined by the proceedings in the second *Chenery* case.

2. In holding that the prior proceedings had conclusively determined as a fact that petitioners' only rights were those of creditors.

3. In applying the strict doctrine of res judicata to the reorganization and merger proceedings of the Securities and Exchange Commission.

4. In affirming the order of the District Court.

## REASONS FOR GRANTING THE WRIT

### I.

### THE DECISION BELOW WARRANTS REVIEW BY THIS COURT TO DETERMINE WHETHER IT ACCORDS PROPER APPLICATION AND SCOPE TO EARLIER DECISIONS OF THIS COURT IN THE PROCEEDINGS.

The court below accords to the decision of this Court in the second *Chenery* case an effect far beyond that which we believe to be warranted, and wholly ignores the probable controlling authority of the first *Chenery* case. Review by this Court is necessary to determine whether its earlier decisions are being given proper scope and application.

The essential facts in this case are, in reality, only two in number. The first fact is that without any fault whatever on petitioners' part, they are being drastically penalized by having all but a small share of the assets allocable to them on the liquidation of Federal turned over, as a windfall, to the other shareholders. The District Court made an explicit finding of absence of fault of any kind (R. 61), and in his memorandum opinion the District Judge said (R. 57) that if he were not, as he thought he was, foreclosed, he—

> "would have no hesitation in holding there is no substantial evidence to support the Commission's finding that Chenery should be penalized".

The District Court's finding was not disturbed by the court below.

The second fact in this case is that petitioners alone have been so penalized. The "rule" which the Commission found in the Holding Company Act, and which was "formulated" as a "standard" and applied, *ex post facto,* in the second *Chenery* case, was immediately abandoned; management stock purchases during reorganization proceedings since the *Chenery* case have not been proscribed or punished (R. 56). Again, the District Judge forcefully states the point (R. 56):

> "Chenery successfully shows that the policy of the Commission—to prohibit and penalize purchases of stock by officers and directors during reorganizations—was only an avowed policy in that it was never followed by the Commission, except in the instant case; * * *"

Again, the court below appears to concur (R. 325).

Stated baldly, in other words, petitioners, without fault on their part, are being singled out for drastic penalties under a "rule" or "standard" which makes absence of fault in the particular case irrelevant, but which did not exist, except to punish them alone. The court below has approved an injunction compelling petitioners to accept that result, solely because of the alleged binding effect of this Court's decision in the second *Chenery* case. We believe it does not compel, and indeed does not support, such an obvious and gross injustice.

1. The Court, in the second *Chenery* case, was led to its conclusion by the representations of the Commission, in its opinion and in its briefs, that the Commission was stating a new rule or standard of conduct derived from the Holding Company Act, making absence of fault in the particular case irrelevant. In the first

*Chenery* case, in which the Court found the order penalizing petitioners unsupportable in the absence of such a rule, the opinion pointed out the possibility which the Commission later purported to adopt (318 U. S. at p. 92):

> "Had the Commission, acting upon its experience and peculiar competence, promulgated a general rule of which its order here was a particular application, the problem for our consideration would be very different."

The Commission's 1945 opinion thereupon discovered a rule which would make absence of fault in the particular case irrelevant (see R. 153, 160, 163, 165).[2] There is no doubt that this Court, in the second *Chenery* case, so understood the Commission's decision. The Court said (332 U. S. at p. 203):

> "Hence we refuse to say that the Commission, which had not previously been confronted with the problem of management trading during reorganization, was forbidden from utilizing this particular proceeding for announcing and applying a new standard of conduct."

2. However, by the time Federal's plan of dissolution came before the Commission, this "new standard of conduct" had ceased to exist. So far as the records show, it was never applied except against petitioners. In three cases indistinguishable in any material way from the circumstances in which the Commission discovered and applied the "rule" against petitioners, the

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[2] The District Court stated (R. 56): "The Commission's opinion in the Chenery case seems clearly to indicate that the circumstances of such case are not controlling but that all transactions in securities during reorganiations by officers and directors, are prohibited."

Commission permitted reorganization managers, who purchased stock during the pending of a plan, to participate in that plan on a parity with other holders of the same class of stock. *In the Matter of Cities Service Co.,* October 1, 1947, Holding Company Act Release No. 7720 (R. 202-228); *In the matter of American States Utilities Co.,* October 3, 1947, Holding Company Act Release No. 7721 (R. 228-253); *In the Matter of Middle West Corporation,* December 9, 1947, Holding Company Act Release No. 7905 (R. 254-312), *sub nom. In re North West Utilities Co.,* 76 F. Supp. 63 (D. C. Del. 1948).

In these three cases, the Commission attempted to excuse its failure to apply the "new standard of conduct" by considering actual harm or degrees of potential harm—considerations totally irrelevant to the standard applied to Chenery. In the light of that rationalization by the Commission, the District Court stated (R. 57):

> "If the facts and consequences of a particular case determine whether a penalty should be inflicted, I think it is clear that the plan could not be approved as fair and equitable. This case is by far the strongest on the facts against the imposition of the penalty."[3]

3. In the first *Chenery* case, the Court held that, absent a "general rule", petitioners could not be penalized. Essentially, therefore, the Commission now seeks to achieve the result which this Court refused to sanc-

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[3] The Court should note that even reorganization managers who made stock purchases knowing of the Commission's disapproval thereof in *Chenery,* were permitted parity treatment. In the *Matter of Cities Service Co., supra.* For petitioners, who *are* penalized, the "new standard of conduct" was admittedly wholly *ex post facto.*

tion in the first *Chenery* case. We believe this Court, in the second *Chenery* case, did not intend to sanction mere formalism; when it approved a decision against petitioners by reason of a "new standard of conduct", it did not mean a new standard applicable *only* to petitioners.

We believe that it is necessary and appropriate, therefore, that this Court grant a writ of certiorari to determine whether proper scope and effect is being accorded to its decisions in both the first and second *Chenery* cases, under the facts as they are now shown to exist.[4]

## II.

### The Decision Below Raises Important Questions as to the Scope of the Doctrine of Res Judicata in Proceedings to Which Administrative Agencies Are a Party.

The opinion of the court below lays principal emphasis on the doctrine of *res judicata*. In applying the doctrine under the circumstances of this case, the court

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[4] The Commission has sought to make much of the fact that a few days before petitions for rehearing were denied in the second *Chenery* case, Federal filed a supplement to its petition for rehearing containing the decisions of the Commission in *Cities Service* and *American States* cases, *supra*, which had been decided a few days earlier. Patently, the very limited review accorded to a supplement to a petition for rehearing cannot be compared with the review which can be given on this record, with both findings of fact and an opinion in the District Court, and an opinion of the Court of Appeals. Moreover, the limited time allowed did not permit the full exposition of the Commission's new position; indeed, the third case, the *Middle West* case, *supra*, which served to round out the new doctrine by which the "new standard of conduct" was abandoned, was not decided until about two months after the petition for rehearing had been denied.

has decided important questions as to the proper scope and application of that doctrine which appear to be in conflict with applicable decisions of this Court and of the other Courts of Appeals, or, alternatively, which have not been, but should be, decided by this Court.

*A. THE HOLDING OF THE COURT BELOW THAT THE DECISION IN A MERGER PROCEEDING IS RES JUDICATA AS TO THE ISSUES IN A DISSOLUTION PROCEEDING IS IN PROBABLE CONFLICT WITH THE DECISION OF THE COURT OF APPEALS FOR THE SECOND CIRCUIT IN THE EVERGREENS V. NUNAN,* 141 F. (2d) 927.

Prior decisions of this Court in the first and second *Chenery* cases dealt with the rights of petitioners under a merger plan—whether the plan was fair and equitable to all persons affected by it and appropriate to effectuate the purposes of the Holding Company Act. Petitioners, had they been allowed parity treatment, would have held 10.1 percent of the voting power (R. 142) which is made presumptive "control" by the Act; control of the future operations and conduct of the reorganized companies was therefore a dominant factor.

The dissolution of Federal is a wholly new matter. It presents no question as to "control" of utility operations. The narrow—and different—question in the present proceeding is simply: who is entitled to Federal's assets after its debts have been satisfied. The previous issue before the Commission centered about the terms and conditions upon which it would be fair, under the Holding Company Act, *to operate* new properties. The present issue goes to the terms and conditions under which it will be fair and equitable *to distribute its assets in liquidation, to cease all operations.* The fundamental requisite of *res judicata*—identity of issues—is lacking.

The court below, however, has nevertheless made the merger proceeding controlling by asserting that "facts"

found in the merger case are now beyond judicial re-examination. The court below stated (R. 324):

> "It is the fact that they are entitled only to claim as creditors and not as stockholders which is res judicata."

Patently, the actions which petitioners maintained in the first and second *Chenery* cases did not seek adjudication of the issue whether they were stockholders or creditors. The issue, simply, was whether petitioners should receive the same as, or less than, other shareholders of the same class in the exchange contemplated by the merger. No order of the Commission has ever required them to turn in their stock, and they still hold it. The extent of their participation in the assets upon the dissolution of Federal was not an issue which was or could have been dealt with in the merger proceedings—an essential prerequisite to the application of the doctrine of res judicata. *Angel* v. *Bullington*, 330 U. S. 183, 192-193.

If it is possible to say—and we doubt it—that the decision in the second *Chenery* case "determined" that petitioners were creditors, it can be only on the ground that such a conclusion must logically follow from the actual decision—that petitioners should not share *pari passu* in the merger. But the decision of the court below giving to such a "fact", thus derived only from alleged logical relevance, the status of a matter which is res judicata, is then in conflict with the decision of the Court of Appeals for the Second Circuit in *The Evergreens* v. *Nunan*, 141 F. (2d) 927 (1944). In that case, the issue was likewise as to the conclusive character, by operation of res judicata, of a certain fact logically derived from the decision in an earlier case. In the earlier case, in determining the value of fully im-

proved cemetary lots, the Tax Court had also "determined" the cost of improving the lots. In the later case, the taxpayer urged that the earlier determination as to the cost of improving the lots was res judicata. The Court rejected the contention. It stated (141 F. (2d) at p. 929):

> "It is altogether right that the judgment shall forever put an end to the first cause of action; but it is not plain that it is always fair that every fact—'ultimate' or 'mediate datum'—decided in it, shall be conclusively established between the parties in all future suits, just because the decision was necessary to the result. * * * There is no reason for subjecting the loser to such extravagant hazards; unless the decisions compel us to go so far, we will not do so."

The Court should grant a writ of certiorari to resolve this conflict in the decisions of the Courts of Appeal, and to make plain the extent to which res judicata is applicable in such circumstances.

*B. THE DECISION BELOW RAISES IMPORTANT QUESTIONS AS TO THE PROPER APPLICATION OF THE PRINCIPLES OF RES JUDICATA TO ADMINISTRATIVE PROCEEDINGS, PARTICULARLY IN THE LIGHT OF THE ADMINISTRATIVE PROCEDURE ACT WHICH HAVE NOT BEEN, BUT SHOULD BE, DECIDED BY THE COURT.*

As we have shown in the preceding section, the issues before the Commission in respect to Federal's dissolution plan were not identical with those litigated in the previous merger proceeding and there is, therefore, no proper factual basis for the application of res judicata. Even if the issues were the same, however, we believe that the decision of the court below refusing to reexamine the issues raises an important question as to the proper application of res judicata in administrative proceedings, particularly in the light of the Administrative Procedure Act.

The decision below, which applies the strict rule of res judicata to a rule-making function, appears to conflict with the many decisions which have considerably limited the doctrine of res judicata in administrative proceedings. *E. g. Securities and Exchange Commission* v. *Otis & Co.,* 338 U. S. 843 (subordinated to requirement of exhaustion of administrative remedies); *Wilbur* v. *United States,* 281 U. S. 206 (Secretary of Interior's decision on Indian claim on land patents not binding on his successor because made in exercise of administrative authority); *West* v. *Standard Oil Co.,* 278 U. S. 200 (Secretary of Interior permitted to revoke previous decision and redetermine whether certain land was known to have mineral deposits); *United States* v. *Stone & Downer Co.,* 274 U. S. 225 (res judicata not applicable to determinations under custom laws); *Pearson* v. *Williams,* 202 U. S. 281 (immigration authorities allowed to rectify earlier error); *Lum Mon Sing* v. *United States,* 124 F. 2d 21 (9th Cir. 1941) (same); *Grandview Dairy* v. *Jones,* 157 F. (2d) 5 (2d Cir. 1946) (eligibility for allowance under milk marketing agreement may be redetermined by Milk Administrator); *Sprague* v. *Woll,* 122 F. (2d) 128 (7th Cir. 1941) (ICC not bound by prior final decision that railroad was entitled to exemption from regulation); *Greater Kampeska Radio Corp.* v. *Federal Communications Commission,* 108 F. (2d) 5 (App. D. C. 1939) (initial finding that broadcast permit holder was qualified may be reversed); *Froeber-Norfleet* v. *Southern Railway Company,* 9 F. Supp. 409 (D. C. Ga. 1934) (ICC determination that certain rates are reasonable does not permit reconsideration and finding of unreasonableness when intervening Commission order in a separate docket is inconsistent); *Di Donato* v. *Rosenberg,* 256 N. Y. 412, 176 N. E. 822

(1931) (State Industrial Board permitted to vacate previous award notwithstanding court approval of that award).

Courts have recognized, in other words, as have commentators, that much of the basis for the inexorable application of res judicata disappears when a regulatory agency is party to the litigation.[5] Agencies have a continuing jurisdiction to legislate, regulate and enforce broadly with respect to various areas of business, are more readily accessible than courts, and often by statute assume the burden of litigation that would otherwise be private. All of these factors, and a growing recognition that it is more important that errors be rectified and justice be achieved rather than sacrificed to the objective of terminating litigation, have served to qualify and delimit the application of res judicata.[6]

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[5] See Griswold, *Res Judicata in Federal Tax Cases*, 46 Yale L.J. 1320 (1937); Davis, *Res Judicata in Administrative Law*, 25 Texas L. Rev. 199 (1947); Schopflocher, *The Doctrine of Res Judicata in Administrative Law*, 1942 Wis. L. Rev. 5, 198; *Res Judicata and Intra-Governmental Inconsistencies*, 49 Col. L. Rev. 640 (1949). In a petition for certiorari in *Securities and Exchange Commission* v. *Otis & Co.*, 338 U. S. 843 (No. 244, Oct. 1949), the Commission itself has admitted (pp. 14-15):

> "The Commission did not argue, as the court below apparently suggests (R. 79-80) that the doctrine of *res judicata* is not applicable to administrative agencies, though when and under what circumstances it is applicable are exceedingly complex questions toward the solution of which the courts are still finding their way. See Davis, *Res Judicata in Administrative Law*, 25 Tex. L. Rev. 199; *Res Judicata and Intra-Governmental Inconsistencies*, 49 Col. L. Rev. 640."

[6] The language of the Court of Appeals for the District of Columbia expresses the weight to be given the element of continuing jurisdiction of administrative agencies:

> "It is for this reason we hold against the contention of petitioner's and not because of lack of any of the elements

Indeed, in its own decision in this proceeding, the Commission expressly declined to hold that it was bound by res judicata (R. 19).

Moreover, the decision below raises important questions which have not been, but should be, settled by this Court as to the application of the Administrative Procedure Act.

Presumably there is no dispute that the doctrine of res judicata is inapplicable to quasi-legislative proceedings. *Prentis* v. *Atlantic Coast Line,* 211 U. S. 210; *Sprague* v. *Woll,* 122 F. (2d) 128 (7th Cir. 1941). The court below, however, held that in the proceedings in the merger case, the Commission was acting in a quasi-judicial capacity (R. 323). That decision not only appears to be in error, but it raises important questions under the Administrative Procedure Act.

Section 2 of that Act distinguishes between the *adjudicatory* function, in performing which the agency acts as a court subject to the traditional rules of court process, and the *rule-making* function, in which the agency legislatives within the limits of its delegated authority. Section 2(c) defines "rules and rule making" as follows:

> " 'Rule' means the whole or any part of any agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or to describe

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which usually make out a case for the application of res judicata. The doctrine is not to be used where the circumstances create a semblance of conditions for its application but to apply it would submerge the plan of Congress for the administration and enforcement of its policy." *Denver Building & Construction Trades Council* v. *NLRB,* 186 F. (2d) 326, 332 (1950).

> the organization, procedure, or practice requirements of any agency and includes the approval or prescription for the future of rates, wages, corporate or financial structures or reorganizations thereof, prices, facilities, appliances, services or allowances therefor or of valuations, costs, or accounting, or practices bearing upon any of the foregoing. 'Rule making' means agency process for the formulation, amendment, or repeal of a rule." 5 USCA Sec. 1001(c), 60 Stat. 237 (1946).

In the same category, therefore, with the prescription of rates, which was a function squarely held *not* to give rise to res judicata in the *Prentis* case, is "prescription for the future of * * * corporate or financial structures or reorganizations thereof" whether "of general or particular applicability". This, indeed, was the recommendation of the Securities and Exchange Commission to Congress.[7]

We do not suggest, of course, that matters be relitigated forever when a merger or reorganization is involved, or an agency is a party. We *do* suggest that there has been a recognition that the law or facts often change so as to make it fair to redetermine an issue after it has once been decided. Whether, in this case, the court below was correct in flatly refusing, because of res judicata, to take those factors into account (see R. 325), we submit is an important question warranting review by this Court.

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[7] See Foster, *Application of the Administrative Procedure Act to the Statutes Administered by the Securities and Exchange Commission* in Federal Administration Procedure Act and the Administrative Agencies (NYU School of Law Institute—Proceedings, Vol. VII) pp. 245-246 (1947).

*C. THE DECISION BELOW IS IN PROBABLE CONFLICT WITH THE DECISION OF THIS COURT IN COMMISSIONER V. SUNNEN,* 333 U. S. 591.

In *Commissioner* v. *Sunnen,* 333 U. S. 591, a taxpayer had assigned his interest in certain royalty agreements to his wife and thereafter all payments due under such agreements were made to her. The Board of Tax Appeals had earlier held that the taxpayer was not taxable on the amounts paid to his wife during the years 1929-1931. Subsequently, the taxpayer's liability for the years 1937-1941 came before the Tax Court. During those years income from royalty agreements made by the taxpayer had been paid to his wife (a) under the very same agreements and assignments that were the subject of the Board of Tax Appeals ruling for the years 1929-1931, and (b) under additional agreements and assignments entered into subsequent to 1931, but identical with the earlier ones in all significant respects. The Tax Court held that res judicata prevented inclusion in the taxpayer's income for 1937-1941 payments to his wife made under the same agreements ruled upon in the earlier determination. It determined, however, that there should be included in his income payments made to his wife under the subsequent agreements. The basis for this change in ruling was a line of cases that had been decided by the Supreme Court subsequent to the Board of Tax Appeals' earlier decision which sharply limited a taxpayer's opportunity to avoid tax by assigning or transferring income to others, especially members of his family, *e.g. Helvering* v. *Clifford,* 309 U. S. 331 (1940); *Helvering* v. *Horst,* 311 U. S. 112 (1940).

This Court, upon review of the Tax Court's action, held that all of the 1937-1941 royalty payments could properly be taxable to the taxpayer. The Court's analysis of the fundamental policy behind res judicata

and its corollary doctrine, collateral estoppel or estoppel by judgment, and its explanation of why that policy must be subordinated to more important objectives, appears to be wholly at odds with the decision below.

As to the tax liability under the later agreements, the Court held that the issue of tax liability in the latter years was sufficiently different from the question of tax liability in the earlier years as not to bar redetermination of the issues once decided. It said (333 U. S. at p. 601):

> *"But if the relevant facts in the two cases are separable, even though they be similar or identical, collateral estoppel does not govern the legal issues which recur in the second case.* Thus the second proceeding may involve an instrument or transaction identical with, but in a form separable from, the one dealt with in the first proceeding. In that situation, *a court is free in the second proceeding to make an independent examination of the legal matters at issue. It may then reach a different result or, if consistency in decision is considered just and desirable, reliance may be placed upon the ordinary rule of stare decisis."* (Emphasis added.)

Certainly, in this case, a proceeding to determine the terms upon which a corporation shall continue to operate is different and separable from one to determine the terms upon which it will be permitted to distribute its assets and dissolve.

The Court went further, however, and held that tax liability under the very contract which the Tax Court had already passed upon could be re-examined because of the intervening legal developments. In this respect the Court said (333 U. S. at p. 603):

> "A more difficult problem is posed as to the $4,881.35 in royalties paid to the taxpayer's wife

> in 1937 under the 1928 contract. Here there is complete identity of facts, issues and parties as between the earlier Board proceeding and the instant one. The Commissioner claims, however, that legal principles developed in various intervening decisions of this Court have made plain the error of the Board's conclusion in the earlier proceeding * * *. It must therefore be determined whether this *Clifford-Horst* line of cases represents *an intervening legal development which is pertinent to the problem* raised by the assignment of the 1928 agreement and which makes manifest the error of the result reached in 1935 by the Board. *If that is the situation, the doctrine of collateral estoppel becomes inapplicable."* (Emphasis added.)

Enough has already been stated to indicate the applicability of the *Sunnen* case here. The Commission, no less than the Commissioner of Internal Revenue, is charged with continuing enforcement of an important policy of Congress. That enforcement involves a nice balancing of public and private interests. It is equally contrary to the interests of good administration, in each case, to perpetuate discriminations and inequities by a blind application of res judicata or collateral estoppel.

In the present case, the basis for re-examination is overwhelming. The unique circumstances which point so strongly to the existence of one rule for petitioners, and a totally different rule for everybody else do not merely warrant redetermination; they demand such redetermination in the interests of fair play and equality under the law.

## CONCLUSION

Wherefore, for the several reasons stated above, the petition for certiorari should be granted.

Respectfully submitted,

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April 30, 1951.

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# In the Supreme Court of the United States

OCTOBER TERM, 1950

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No. 709

CHENERY CORPORATION, ET AL., PETITIONERS

*v.*

SECURITIES AND EXCHANGE COMMISSION

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*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT*

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## MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

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### OPINIONS BELOW

The opinion of the court below (R. 317-326) has not yet been reported. This Court's prior denial of certiorari is reported at 340 U.S. 831. The opinion of the District Court is reported at 87 F. Supp. 289. The opinion and findings of the District Court appear at R. 52-68.[1] The findings and opinion of the Commission

[1] The letter "a" which is included as part of the number of each page of the Joint Appendix in accordance with the rules of the Third Circuit has been omitted herein.

(R. 7-31) are reported in Holding Company Act Release No. 8313, and the supplemental findings and opinion of the Commission (R. 34-38) are reported in Holding Company Act Release No. 8387.

### JURISDICTION

The judgment of the court below was entered on April 2, 1951 (R. 327). Petitioners invoke the jurisdiction of this Court under 28 U.S.C. 1254(1).

### QUESTION PRESENTED

Whether the Court of Appeals erred in affirming an order of the district court approving and enforcing pursuant to Section 11(e) of the Holding Company Act a plan for the liquidation of a holding company which, as approved by the Commission in 1948, accorded petitioners the precise amount which the Commission had approved in an earlier plan for the reorganization of predecessor companies in the 1945 order affirmed pursuant to this Court's mandate in *S. E. C.* v. *Chenery Corporation,* 332 U. S. 194 (the second *Chenery* case).

### STATUTES INVOLVED

Sections 11(e) and 18(f) of the Public Utility Holding Company Act of 1935, 15 U.S.C. §§ 79k(e) and 79r(f) are printed in the petition at pages 2-4.

### STATEMENT

An understanding of the issues presented by this petition will be facilitated, we believe, by distinguishing two separate administrative proceedings in which petitioners have participated; first, a reorganization

or merger proceeding—twice before this Court—affecting stockholders of the former Federal Water Service corporation,[2] and, second, the instant proceeding for court enforcement of a later plan for the liquidation of Federal Water and Gas Corporation, the company which survived the merger.

On March 24, 1941, the Commission issued findings in the merger proceeding indicating approval of Federal's then proposal with respect to the allocation of the new common stock among the public security holders of the old company, but disapproving the plan in its then form insofar as it provided for participation, on a basis of parity with the old company's other preferred stock, of preferred stock purchased individually by the management (Chenery et al.) during the course of the proceeding (R. 93.)[3]

Thereupon a new Paragraph Fourth (d) was added to the merger agreement, providing that Chenery et al. were to receive no new stock in respect of their preferred shares purchased after November 8, 1937,[4] but merely cash equal to their cost plus interest at 4%

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[2] The prior proceeding involved the merger into Federal Water Service Corporation of its parent company, Utility Operators Company, and a wholly owned subsidiary, Federal Water and Gas Corporation, the creation of a simplified capital structure consisting of debt and common stock only, and the renaming of the surviving corporation as Federal Water and Gas Corporation.

[3] *Federal Water Service Corporation*, 8 S.E.C. 893 (1941).

[4] Prior to registration in November 1937, including the months immediately prior to registration when reorganization plans were being formulated and discussed, Chenery et al. had also purchased shares of the preferred stock of Federal Water Service Corporation. Certain of those purchases were criticized by a stockholder who participated in the merger proceeding (R. 140), but those shares were permitted to participate on a parity with publicly held shares (R. 135), and the treatment accorded them is not now in dispute.

to the effective date of the merger agreement. The merger plan as so amended was approved by the Commission over the objection of Chenery et al. on September 24, 1941 (R. 117).[5]

The merger plan did not contemplate court enforcement but was to be consummated under state merger procedure requiring a favorable vote of each class of stockholders affected. Accordingly, Section 11(g) of the Holding Company Act subjected to Commission supervision the company's solicitation of votes for the plan and required distribution in connection therewith of a report by the Commission on the plan. Such a report was distributed along with a letter from C. T. Chenery as President of the Company. Both this letter (R. 121) and the Commission's report (R. 117-118) discussed the Commission's decision, described the new provisions of the merger agreement limiting Chenery et al., in respect of the stock in controversy, to cost and interest, and referred to the possibility of proceedings to review that decision. The letter refers to the plan as one "which required all persons [connected with the management] who, after November 8, 1937, purchased Preferred stock * * * to surrender the stock so purchased to the Corporation" at cost plus 4% per annum (R. 122), but notes:

> If, on appeal by such officers or directors, it should be held that the Securities and Exchange Commission has acted illegally and beyond its authority in this matter, it is believed that such Preferred stock should be permitted to participate in the reorgani-

[5] *Federal Water Service Corporation*, 10 S.E.C. 200 (1941).

zation on the same basis as other Preferred stock [R. 124].

At the stockholders' meeting of the corporation, Chenery et al. accompanied their votes against the merger with letters which stated, *inter alia:*

> * * * I hereby state with the intention that this statement should be relied upon by the Board of Directors of Federal Water Service Corporation in deciding whether to declare the merger agreement operative that
>
> (1) *if,* in the proceeding taken by the interveners to review the order of the Securities and Exchange Commission, *it is finally determined that said order shall be affirmed, I will surrender my stock* referred to in paragraph FOURTH (d) of the merger agreement to the surviving corporation *for cancellation* for the consideration set forth in paragraph FOURTH (d) of the merger agreement; [R. 126-127. Emphasis supplied.]

A requisite majority of the stockholders voted favorably on the plan, the directors declared it operative, and on October 31, 1941 the merger was fully consummated (R. 125). The old stocks of the merging companies were cancelled, and the new common stock of Federal Water and Gas Corporation was issued. Thus the statement by petitioners (p. 16) that they hold preferred stock in Federal Water Service Corporation is true only in the sense that they are in physical possession of certain old certificates.

Upon a petition for review filed by Chenery et al., this Court held that the equitable precedents relied

upon by the Commission were inapplicable, intimated that the Commission's order might perhaps be sustainable upon grounds not explicated in its opinion, and ordered the case remanded to the Commission for further proceedings not inconsistent with this Court's decision. *S. E. C.* v. *Chenery Corporation,* 318 U. S. 80.

After the remand the surviving company, of which C. T. Chenery was (and still is) the principal executive officer, proposed an amendment to the merger plan based upon the view that the first *Chenery* case required the Commission to accord Chenery et al. equal treatment with public holders of the preferred stock of the old company. In 1945 the Commission entered a new decision (R. 131-173, 63) [6] rejecting that amendment and reapproving the merger plan as of September 24, 1941, in the form which had been approved in the 1941 order set aside in the first Chenery litigation. The Commission stated that the decision was based upon its administrative judgment and experience as applied to the specific facts of the case. Upon review this Court on June 23, 1947, upheld the Commission's action and remanded the case to the Court of Appeals for the District of Columbia for the entry of a judgment and decree. *S. E. C.* v. *Chenery Corporation,* 332 U. S. 194.

On July 16, 1947, Chenery et al. (R. 177) and Federal Water and Gas Corporation (R. 174) filed petitions for rehearing in this Court. On October 8, 1947, Federal Water and Gas Corporation filed with this Court a supplement to its petition for rehearing (R. 179). In

[6] *Federal Water Service Corporation,* 18 S.E.C. 231 (1945).

these petitions substantially the identical arguments were presented that now form the basis for the present petition. Chenery argued then that this Court "has made no holding as to whether or not the provision of the plan whereby the Chenery Corporation and the other interveners are required to surrender their stock at cost plus four per cent interest is 'fair and equitable'" (R. 177). The same *Cities Service* and *American States* decisions, which petitioners here allege to be inconsistent with the Commission's *Chenery* decision, were cited to this Court, and it was argued:

> In view of these decisions * * * we do not see how this Court can allow its decision in the *Chenery Corporation* case to stand. There has been what may be described as an administrative hoax. * * * These new decisions on the part of the Commission sweep away the entire basis for this Court's decision and raise new questions as to the interpretation of this Court's opinion which, it is respectfully submitted, should be settled by this Court. [R. 180-181].

The petitions for rehearing were denied on October 13, 1947. 332 U. S. 783.

On July 22, 1947, this Court issued its mandate to the United States Court of Appeals for the District of Columbia (R. 178). On or about October 23, 1947, the Clerk of the Court of Appeals submitted to all counsel a draft of a proposed judgment and decree fully affirming the Commission's order (R. 181). Counsel for Chenery et al. and for Federal Water and Gas Corporation opposed the proposed judgment and decree (R.

182-189), and urged that the case be either remanded to the Commission "for further proceedings in conformity with the opinion of the Supreme Court" (R. 182, 189) or that the Commission's order only be affirmed "in so far as it denied the application of Federal Water and Gas Corporation for leave to amend the merger agreement." (R. 183). They stated that if the Court should affirm the Commission's order of February 7, 1945, "It will no doubt be contended by the Securities and Exchange Commission that the judgment of the Supreme Court is res adjudicata as to the fairness and equity of the corporation's depriving the interveners of their stock upon payment of cost plus 4% interest." (R. 186). The Commission filed with the Court of Appeals a memorandum in opposition to these suggested modifications of the proposed judgment and decree (R. 189), urging the issuance of a decree and mandate constituting a full affirmance of the Commission's order. The Commission stated:

> Of course, the Commission would contend that affirmance of its order under review would be a conclusive determination of the fair and equitable issue. * * * The fact that affirmance would under the statutory scheme give finality to the Commission's order is, we submit, an additional reason for entering an order of affirmance unless there appears to be some warrant for setting aside the order, and, as stated above, we believe that the Supreme Court's opinion precludes a reversal in whole or in part. [R. 199.]

On December 12, 1947, the Court of Appeals entered a decree and mandate in substantially the form originally proposed and in accordance with the Commission's recommendation, which set aside and annulled its prior reversal of the Commission's order and provided:

> IT IS FURTHER ORDERED AND DECREED by this Court that the order of the Securities and Exchange Commission issued February 7, 1945, in these cases be, and is hereby, affirmed. [R. 65.]

The final step in connection with the merger proceeding was a petition dated January 19, 1948, by Chenery et al. to the Commission for rehearing, reconsideration, and modification of its order of February 7, 1945 (R. 93). This was denied by the Commission by order dated February 5, 1948 (R. 201). No review of that order was sought.

Meanwhile on December 31, 1942, the new Federal Water and Gas Corporation, created by the 1941 merger, had filed with the Commission a plan pursuant to Section 11(e) of the Act under which it would cease to exist by dissolution or otherwise. The proceeding on said plan was consolidated with proceedings instituted by the Commission with respect to the new corporation pursuant to Section 11(b) of the Act. Parts of said plan were approved by order of the Commission dated February 10, 1943.[7] A number of supplemental plans, applications, and declarations, not now in dis-

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[7] *Federal Water and Gas Corporation*, 12 S.E.C. 766.

pute, were filed in the consolidated proceedings and were acted upon by the Commission from time to time.

On November 7, 1947, Federal Water and Gas Corporation filed with the Commission pursuant to Section 11(e) of the Act, an Amended and Supplemental Plan providing specific steps to accomplish its dissolution. This dissolution plan of the new corporation, filed subsequent to this Court's decision in the second *Chenery* case, treated as still undecided the amount that Chenery et al. should receive by virtue of their former interest as preferred stockholders in the old company (R. 5-6).

On July 2, 1948, the Commission entered its Findings and Opinion (R. 7-32) in the dissolution proceeding, finding that the plan could be approved if amended in certain respects, including a provision for payment to Chenery et al. of the amount determined in the merger proceeding.[8] The Commission stated that "there has been a final determination upheld on judicial review, that the payment of $313,190 in full satisfaction of the claims of Chenery et al. would be fair and equitable" (R. 18), and that "the original security claims of Chenery et al. have been transmuted into and must now be regarded as claims against Federal for an amount of $313,190" (R. 18). The Commission held that even if the principle of *res judicata* were not a bar to re-examination of the question, and even if the matter were one in which, due to changed conditions, the exer-

[8] Such payment was to constitute full discharge of all claims of Chenery, et al., unless they should succeed in having the Commission decision overruled by the courts in this proceeding for enforcement of the dissolution plan (R. 23).

cise of discretion and reconsideration were permissible, there were no such new considerations or circumstances which would require a different result (R. 19). The dissolution plan as subsequently amended to conform to that opinion was approved by the Commission on July 27, 1948 (R. 34).

On July 28, 1948, the Commission applied to the District Court of the United States for the District of Delaware for enforcement of the plan (R. 3). On August 19, 1948, Judge Leahy of that Court, without opposition, ordered enforcement of the plan in all respects except as to Section 3 of the amended plan which provided that the payment by Federal of $313,190 to Chenery et al. would be in full satisfaction of their claims (R. 1). Hearings on that issue were held on October 25, 1948, and September 16, 1949. On December 2, 1949, Judge Leahy entered a memorandum opinion (R. 52), holding himself bound by this Court's decision to find the plan fair and equitable and enforce it, but stating:

> Consequently, if I did not think I were foreclosed by the Supreme Court, as detailed above, I would have no hesitation in holding there is no substantial evidence to support the Commission's finding that Chenery should be penalized and limited to cost plus interest for its preferred stock purchases [R. 57].

On January 11, 1950, the District Court issued an order (R. 58) approving Section 3 of the plan as fair and equitable and appropriate to effectuate the pro-

visions of Section 11 of the Act and ordered the plan enforced. Petitioners appealed from that order to the Court of Appeals for the Third Circuit, and then petitioned this Court for certiorari before hearing by the Court of Appeals, which petition was denied on October 9, 1950. After review by the Court of Appeals, it affirmed the order of the district court on April 2, 1951. The present petition is for review of that decision.

ARGUMENT

The court below properly held that the doctrine of *res judicata* was applicable to this much litigated case. Petitioners' contention that the Commission has abandoned in subsequent decisions the doctrine enunciated in *Chenery* is unfounded. There is no conflict of decisions. We think it high time that this litigation involving transactions occurring between 1937 and 1940 was brought to a close.

1. The Commission did not err in refusing to reexamine and modify, assuming it had power to do so, the decision which was affirmed, in response to the mandate of this court in the second *Chenery* decision. Petitioners' sole ground for reopening the earlier decision is the contention that subsequent administrative rulings involve an abandonment of the "rule" which the Commission applied to Chenery et al. This argument—apart from its irrelevance—rests upon a misinterpretation of Commission decisions, of which the more significant were called to the attention of this Court in connection with the petition for rehearing in the second *Chenery* case.

The Commission has not abandoned the view that actual wrongdoing need not be proved; it has merely held that absent actual wrongdoing, the degree of conflict of interest and the likelihood of harm to public investors may be examined in the individual case, and that when the conflict is less acute than in the *Chenery* situation, a different result may be justified. Thus the *Cities Service* opinion, after carefully examining the facts, refers to "the conclusion we have reached that the trading here involved did not create a conflict as acute or carry as great a degree of potential danger in [*sic*] the interests of other investors and to the integrity of the reorganization process as that created by the concerted purchase program involved in the *Federal Water Service* case." (R. 222-223). Indeed, the *Chenery* case itself recognized that the problem was one of degree.[9] The Court is respectfully referred to the opinions of the Commission in the later cases involving management purchases, where the grounds of distinction are spelled out at length (R. 218-223, 237-246, 290-294, 18-22).[10]

Petitioners now rely particularly on the *Middle West* case because this case was decided after this issue of alleged administrative inconsistency was previously called to the attention of this Court. It is stated (p. 14, n. 4) that this case "served to round out the new doctrine." That case, however, rests upon a distinction of

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[9] See footnote 4, *supra*, p. 3.

[10] We might point out again that these same charges of inconsistency have previously been urged upon this Court in the petition for rehearing (R. 179-181) which this Court denied in 1947.

degree drawn in the *Chenery* case itself, since both in *Chenery* and in *Middle West* the Commission refrained from imposing the sanction of limitation to cost in the case of securities purchased prior to the reorganization proceedings, but when reorganization could have been anticipated. All purchases involved in *Middle West* were in this category (R. 292-293. See also fn. 4, *supra*).

The Commission still believes, as it argued in the *Chenery* case, that it is not feasible to anticipate and cover by an all-inclusive rule the varying situations in which the proper discharge of a fiduciary obligation precludes the fiduciary from engaging in conduct for personal profit because of the conflicting interest created by such collateral activity. At the same time the Commission is, and has been, conscious of the element of retroactivity in applying an ethical judgment after the event. The choice between these two conflicting considerations, although productive of differences of opinion in its application, is one which this Court has held to lie within the Commission's statutory responsibility, stating "the choice made between proceeding by general rule or by individual, *ad hoc* litigation is one that lies primarily in the informed discretion of the administrative agency." (332 U.S. at 203).

Even if, contrary to our view, the post-*Chenery* decisions had been more lenient than the *Chenery* case in applying the Commission's policy of discouraging trading by fiduciaries in securities affected by a reorganization, this would at most indicate that there has been

heed for this Court's admonition to proceed with caution in exercising a choice of method within its statutory power. The Commission specifically adverted to this admonition in both the *Cities Service* case (R. 223) and the *American States* case (R. 240).[11]

2. The courts below properly held that petitioners were barred by the doctrine of *res judicata*. The instant plan awards the petitioners payment in full in cash for the precise amount of their interest in the reorganized Federal as determined, and litigated to final conclusion, in the earlier merger proceeding. Since this is an entirely separate proceeding from the original merger case reviewed by this Court, petitioners, in asserting rights as stockholders in the reorganized Federal, are seeking to relitigate in a new suit between the same parties the precise issue finally determined in the prior litigation. Petitioners seek a redetermination of their rights arising out of the very same transactions passed upon in the prior decisions—not to separable though similar transactions such as were involved in *Commissioner* v. *Sunnen*, 333 U.S. 591, 598.[12] We

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[11] That the Commission has not abandoned the policy of discouraging trading by fiduciaries in securities affected by reorganizations is evidenced *inter alia* by its briefs before this Court in Chapter X proceedings. See *Mosser* v. *Darrow*, October Term, 1950, No. 461, decided May 7, 1951; *Manufacturers Trust Co.* v. *Becker*, 338 U. S. 304; *Simonsen* v. *Emmerling*, certiorari denied, 339 U. S. 978.

[12] In tax cases, intervening facts and legal developments may result in the application of different principles to similar tax situations in subsequent years, but no one would contend that such new approach could be used to reassess the taxes for the years in which determinations had already been made—a contention more nearly analogous to the one appellants are making here. The other cases which petitioners cite (p. 18) as in conflict with the de-

believe it would be hard to find a clearer case for the application of the rule of *res judicata.*[13]

While petitioners concede that matters should not be relitigated "forever" (Pet. p. 21), they argue that the type of Commission determination here involved is rule-making, and apparently that any determination so categorized can never be finally adjudicated. The court below properly held, however, that in its proceeding in this case the Securities and Exchange Commission "was not laying down rules of conduct for the future in the exercise of its quasi-legislative power," but on the contrary "was acting in a quasi-judicial or adjudicatory capacity to determine the existing obligations and duties of the holding companies in question and the rights of their creditors and stockholders under the legal standards laid down in the Act and in the light of their past conduct" (R. 323). The court correctly

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cision below fully support the holding that petitioners are barred by *res judicata*. We agree that *res judicata* has only limited application to decisions on the fairness of rates which necessarily differ with changes in the basic economic facts. Similarly the availability of exemptions and the granting of licenses or certificates of necessity, are manifestly only temporary adjudications intended to be revised whenever changed conditions make the earlier holdings inappropriate. *The Evergreens* v. *Nunan*, 141 F. 2d 927 (C.A. 2), which petitioners also allege to be in conflict, is not sufficiently close to the present situation to warrant discussion.

[13] See *Angel* v. *Bullington*, 330 U. S. 183, 192-193, in which the opinion states: "The doctrine of res judicata reflects the refusal of law to tolerate needless litigation. Litigation is needless if, by fair process, a controversy has once gone through the courts to conclusion * * * And it has gone through, if issues that were or could have been dealt with in an earlier litigation are raised anew between the same parties." See also *International Union of Mine, Mill & Smelter Workers* v. *Eagle-Picher Co.*, 325 U. S. 335; *Chicot County Drainage District* v. *Baxter State Bank*, 308 U. S. 371; *United States* v. *Smith*, 331 U. S. 469; *Federal Power Commission* v. *Pacific Power & Light Co.*, 307 U. S. 156.

concluded that when an administrative agency exercises power of this sort "and its order has been affirmed by the final judgment of a reviewing court, the rights and liabilities necessarily determined by the judgment of affirmance become *res judicata" (ibid). International Union of Mine, Mill and Smelter Workers* v. *Eagle-Picher Co.,* 325 U.S. 335.

Petitioners' argument that the Commission's determination constitutes rule-making is predicated upon the definition of "rule" in Section 2(c) of the Administrative Procedure Act (60 Stat. 237, 5 U.S.C. § 1001 (c)) as including "the approval or prescription for the future of * * * corporate or financial structures or reorganizations thereof * * * services or allowances therefor * * *". Even assuming that the Administrative Procedure Act is applicable to this case,[14] it is apparent that its definition of rule-making was enacted only to serve as the basis for the procedural differentiations established in the Act itself. The definition was not intended to have any effect upon the doctrine of *res judicata,* a subject not considered by Congress in the Administrative Procedure Act or elsewhere.

Acceptance of petitioners' argument would mean not only that the treatment of Chenery would be open to reexamination, but that the allocations as between the various classes of public security holders of the old Federal Water Service Company would still be open to reexamination. Indeed, if petitioners are entitled to

[14] The earlier proceedings antedated the Administrative Procedure Act, and accordingly that statute would not apply to them. Section 12, 5 U.S.C. § 1011.

attack collaterally the determination of fairness as to them it is hard to see how any determinations of fairness could settle anything in the Commission's step-by-step simplification of holding company systems. *Cf. S.E.C.* v. *Central-Illinois Securities Corporation*, 338 U.S. 96, 140-142.

3. Federal Water and Gas, although it did not appeal from the order of the district court, supported the appeal below and supports the petition for a writ. Federal urges that the nature of the Commission's 1945 order, involved in the second *Chenery* case, precludes application to it of the doctrine of *res judicata*. This order had two parts, one of which reaffirmed as of its original date the 1941 order, set aside in the first *Chenery* litigation, which limited Chenery, et al. to a cash payment of $313,190.22. The other part of the Commission's 1945 order disapproved a proposal of Federal, made in the form of an amendment to the plan after its return to the Commission, to accord Chenery, et al. stock in the merged company on a parity with the public holders of the old preferred stock. Because the opinions of the Commission and this Court in both *Chenery* cases had emphasized the power and responsibility of the Commission to deny participation in a plan, except as affirmatively satisfied that such participation was in accordance with the applicable statutory standards, Federal, as well as petitioners, argued before the Court of Appeals for the District of Columbia that this Court's mandate in the second *Chenery* case did not warrant unqualified affirmance of both the affirmative and negative parts of the Commission's order. [R. 182-189] Al-

though that argument was rejected by the Court of Appeals, and no attempt was made to bring directly to this Court the controversy as to what the mandate required, Federal now seeks to raise the same issue collaterally. Such an attack is precluded by Section 24(a) which provides: "the judgment and decree of the [Court of Appeals] affirming, modifying, or setting aside, in whole or in part, any such order of the Commission shall be final, subject to review by the Supreme Court of the United States . . ." *International Union of Mine, Mill & Smelter Workers* v. *Eagle-Picher Co.*, 325 U.S. 335 indicates that in such circumstances, under a similar review provision, the Commission itself would lack power to change its decision after affirmance by a reviewing court. In this case, the Commission was presented with a petition for rehearing, reconsideration, and modification after the order of affirmance, and without questioning its jurisdiction to change its ruling, declined to do so (R. 201). No review was sought of that order which was the last step in the merger proceeding.

Federal now urges that this Court in the second *Chenery* case "interpreted the Commission's order as making the findings necessary to support a self-executing 'negative' order" and that this Court did not have before it "the question of the legal rights of petitioners in a 'fair and equitable' reorganization under the Act." It is urged (pp. 9-12) that this Court merely upheld the power of the Commission to "pass a rule" which was allegedly abrogated on October 1, 1947 (the approximate date of the *Cities Service* and *American States*

decisions), since when "there has been no legal impediment to Federal's treating the stock of petitioners in the same way as other stock was treated." While we believe both these arguments were disposed of by the order of affirmance by the Court of Appeals for the District of Columbia, which was entered on December 12, 1947, after the alleged abrogation of the rule, they are in any event without merit. We find nothing in the language of this Court quoted by Federal, or elsewhere in its opinions, which supports the interpretation that this Court was merely rendering an abstract decision with respect to the Commission's power to deal thereafter with the holdings of Chenery et al. as distinguished from passing upon the correctness of the Commission's determination in the particular case which had already limited them to cost plus interest.[11] Moreover, Federal's argument opens up a vista of never-ending litigation with respect to administrative decisions based upon experience, on the ground that such experience "is constantly changing." (p. 14).

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[11] See for example the statement in the second *Chenery* opinion that—"The absence of a general rule or regulation governing management trading during reorganization did not affect the Commission's duties in relation to the particular proposal before it. The Commission was asked to grant or deny effectiveness to a proposed amendment to Federal's reorganization plan whereby the management would be accorded parity treatment on its holdings. It could do that only in the form of an order, entered after a due consideration of the particular facts in light of the relevant and proper standards." (332 U.S. at 201). See also the dissenting opinion which states that the Commission "did not previously promulgate, and it does not by this order profess to promulgate, any rule or regulation to prohibit such purchases absolutely or under stated conditions." (p. 215).

CONCLUSION

This petition does not in our view raise any question calling for further review by this Court. The decision of the Court of Appeals was correct and there is no conflict of decisions. The petition should be denied.

Respectfully submitted,

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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1950

No. 709

CHENERY CORPORATION, *et al.*,
*Petitioners,*

v.

SECURITIES AND EXCHANGE COMMISSION.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

## MEMORANDUM ON BEHALF OF FEDERAL WATER AND GAS CORPORATION

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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1950

CHENERY CORPORATION, *et al.*,
*Petitioners,*
v.
SECURITIES AND EXCHANGE COMMISSION.

No. 709

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

## MEMORANDUM ON BEHALF OF FEDERAL WATER AND GAS CORPORATION

### Opinions Below

The opinion of the District Court is reported in *In re Federal Water & Gas Corporation*, 87 F. Supp. 289 (D. Del. 1949). The findings and opinion of the Commission (R. 7-32) are reported in Holding Company Act Release No. 8318 and the supplemental findings and opinion of the Commission (R. 34-42) are reported in Holding Company Act Release No. 8387. The opinion of the Court of Appeals (R. 317-326) is not yet reported.

### Jurisdiction

The judgment of the Court of Appeals was entered on April 2, 1951 (R. 327). Petitioners invoke the jurisdiction

of this Court under Section 1 of the Act of June 25, 1948, 28 U. S. C. § 1254(1) (Supp. 1949).

**Question Presented**

Whether the decision of this Court in *Securities & Exchange Commission* v. *Chenery Corporation,* 332 U. S. 194 (1947), is *res judicata* of the issues presented by paragraph 3 of the Plan of Liquidation.

**Statutes Involved**

Sections 11(e) and 18(f) of the Public Utility Holding Company Act of 1935, 49 Stat. 822, 832 (1935), 15 U. S. C. §§ 79k(e), 79r(f) (1946), are printed in the petition at pages 2 and 4.

Since the decision of this Court in the prior proceedings also involved Sections 6 and 7 of the Public Utility Holding Company Act, we quote the pertinent parts of these sections. Section 6(a) of the Public Utility Holding Company Act provides:

> "Except in accordance with a declaration effective under section 7 and with the order under such section permitting such declaration to become effective, it shall be unlawful for any registered holding company or subsidiary company thereof, by use of the mails or any means or instrumentality of interstate commerce, or otherwise, directly or indirectly (1) to issue or sell any security of such company; or (2) to exercise any privilege or right to alter the priorities, preferences, voting power, or other rights of the holders of an outstanding security of such company." 49 Stat 814 (1935), 15 U. S. C. § 79f(a) (1946).

Section 7(d) (6) provides:

> "If the requirements of subsections (c) and (g) are satisfied, the Commission shall permit a declaration regarding the issue or sale of a security to become effective unless the Commission finds that— * * * (6) the terms and conditions of the issue or sale of the security are detrimental to the public interest or the interest of investors on consumers." 49 Stat. 816 (1935), 15 U. S. C. § 79g(d) (1946).

Section 7(e) provides:

> "If the requirements of subsection (g) are satisfied, the Commission shall permit a declaration to become effective regarding the exercise of a privilege or right to alter the priorities, preferences, voting power, or other rights of the holders of an outstanding security unless the Commission finds that such exercise of such privilege or right will result in an unfair or inequitable distribution of voting power among holders of the securities of the declarant or is otherwise detrimental to the public interest or the interest of investors or consumers." 49 Stat. 816 (1935), 15 U. S. C. § 79g(e) (1946).

**Statement**

Federal Water and Gas Corporation (including the same corporation under its former name, Federal Water Service Corporation) herein referred to as "Federal" has filed four plans with the Securities and Exchange Commission, for the treatment of the preferred stock owned by petitioners and which was purchased by them during the period from 1937 to 1940 while plans of reorganization for Federal were on file with the Commission.

The first plan proposed the same treatment for the preferred stock of petitioners as was accorded to other preferred stock of the same class. This plan was held to contemplate the issuance of securities on terms that were detrimental to the public interest or the interest of investors and was not fair and equitable. 8 S. E. C. 893 (1941).

The second plan prohibited the issuance of common stock to petitioners in exchange for their preferred stock and provided that they should be entitled on surrender of their certificates of preferred stock to receive an aggregate amount of $313,190.22. This was held to be not detrimental to the public interest or the interest of investors or consumers and presumably fair and equitable. 10 S. E. C. 200 (1941). The order of the Commission permitting this plan to become effective was reversed by the Court of Appeals for the District of Columbia. *Chenery Corporation* v. *Securities and Exchange Commission*, 128 F. (2d) 303 (App. D. C. 1942), and the order of the Commission was set aside pursuant to the mandate of this Court. *Securities and Exchange Commission* v. *Chenery Corporation*, 318 U. S. 80 (1943).

The third plan treated the preferred stock owned by petitioners in the same way as other preferred stock had been treated by the second plan. This was held by the Commission to be detrimental to the public interest or the interest of investors or consumers and not fair and equitable, 15 S. E. C. 849 (1944); 18 S. E. C. 231 (1945). The order of the Commission denying this plan also reaffirmed as of September 24, 1941, the order of the Commission approving the second plan. The reason given in the opinion and order for the reaffirmance was to remove any possible question about the legality of the securities which had been

issued under the second plan. The order of the Commission was reversed by the Court of Appeals for the District of Columbia, *Chenery Corporation* v. *Securities and Exchange Commission*, 134 F. (2d) 6 (App. D. C. 1946), but the order of the Court of Appeals was reversed by this Court, *Securities & Exchange Commission* v. *Chenery Corporation*, 332 U. S. 194 (1947), rehearing denied, 332 U. S. 783 (1947). The Court of Appeals over the objection that the affirmative part of the Commission's order was not passed upon by this Court entered an order on December 12, 1947, affirming the order of the Commission of February 7, 1940 (R. 65a).

The fourth plan—the present one—is part of a plan of liquidation of Federal. It provides for the deposit of $313,190.22 in The New York Trust Company in full satisfaction and discharge of all claims of petitioners growing out of the acquisition of their preferred stock. This plan was held fair and equitable by the District Court for the District of Delaware (87 F. Supp. 289) on the ground that it was compelled to do so by the decision of this Court in the second *Chenery* case, and its decision has been affirmed by the Court of Appeals.

## ARGUMENT

**First: The second Chenery case is based upon the power of the Commission to pass a rule, not to make an adjudication. There is no question of res judicata in this case.**

It was not clear from the opinion of the Commission of March 28, 1941, or the supplemental opinion of the Commission of September 28, 1941, whether the Commission's

order was based upon an alleged adjudication by the Commission of the legal rights of petitioners in a fair and equitable plan of reorganization under the Act, or whether the Commission was exercising its power under the Act to refuse to allow a corporation to issue securities under a reorganization plan upon terms that were "detrimental to the public interest or the interest of investors or consumers." From the statutory standpoint, paragraph Fourth (d) could possibly be looked upon as a condition inserted in the merger agreement in order that the merger agreement might be not detrimental to the public interest or the interest of investors or consumers within the meaning of Section 7. It also could be looked upon as a provision inserted in the merger agreement in order that the merger agreement might be fair and equitable to the parties affected thereby within the meaning of Section 11(e). Since whichever way it was looked upon, the order was not supported by the judicial precedents upon which the Commission relied, the order was set aside. It is plain from the minority opinion that it was considered that the Commission was preventing Federal from consummating a plan which the Commission could properly hold was "detrimental to the public interest or the interest of investors or consumers." Treating the opinion of the minority on the first review as the opinion of the majority on the second review, the opinion of the majority on the second review is perfectly clear when it said (332 U. S. 194, 196):

> "* * * On remand, the Commission reexamined the problem, recast its rationale, and reached the same result. * * *"

The result referred to is the refusal of the Commission, as indicated by its opinion of March 24, 1941, to approve

a reorganization plan which treated the stock owned by petitioners in the same way as other stock was treated and otherwise than on a basis of cost.

The question presented by Federal's application for leave to amend the merger agreement (the third plan) was the same as the question presented by the reorganization plan which was considered by the Commission in its opinion of March 24, 1941 (the first plan). It was not necessary for the Commission in the view of the Court to adjudge the legal rights of petitioners. It was only necessary to determine whether the Congress had authorized the Commission to take into consideration in determining whether a plan of reorganization or an amendment to the plan was detrimental to the public interest or the interest of investors the fact that the securities were purchased by fiduciaries while a plan was on file with the Commission and whether such circumstance justified a new rule or policy prohibiting benefits or profits to be obtained out of the approval by the Commission of the reorganization. Federal, in substance, had applied for a license to reorganize. The Commission felt that the license ought not to be granted except on conditions for the protection of the public interest. It had made an error of law in its first decision which was pointed out by the Court on the first review. This Court accordingly applied the principle of *Federal Communications Commission* v. *Pottsville Broadcasting Co.*, 309 U. S. 134 (1940), saying (332 U. S. at 200-201):

> "* * * The fact that the Commission had committed a legal error in its first disposition of the case certainly gave Federal's management no vested right to receive the benefits of such an order. See *Federal Communications Commission* v. *Pottsville Broad-*

> *casting Company,* 309 U. S. 134, 145. After the remand was made, therefore, the Commission was bound to deal with the problem afresh, performing the function delegated to it by Congress. It was again charged with the duty of measuring the proposed treatment of the management's preferred stock holdings by relevant and proper standards. Only in that way could the legislative policies embodied in the Act be effectuated. *Cf. Labor Board* v. *Donnelly Co.,* 330 U. S. 219, 227-228."

Again (p. 201):

> "* * * The Commission was asked to grant or deny effectiveness to a proposed amendment to Federal's reorganization plan, whereby the management would be accorded parity treatment on its holdings. It could do that only in the form of an order, entered after a due consideration of the particular facts in light of the relevant and proper standards. * * *"

It is unnecessary to labor the point. The Court at no place indicated that the Commission's decison was "authorized" by Section 11(e) of the Act. The Court said (p. 207):

> "* * * Our duty is at an end when it becomes evident that the Commission's action is based upon substantial evidence and is *consistent* with the authority granted by Congress. See *National Broadcasting Co.* v. *United States,* 319 U. S. 190, 224" (Italics supplied).

The statement in the *National Broadcasting Co.* case to which reference is made is (319 U. S. at 224):

> "* * * Our duty is at an end when we find that the action of the Commission was based upon findings

supported by evidence and was made *pursuant* to authority granted by Congress. * * *" (Italics supplied).

The citation by this Court of the cases of *United States* v. *Lowden*, 308 U. S. 225 (1939), and *Interstate Commerce Commission* v. *Railway Labor Executives Assn.*, 315 U. S. 373 (1942), both of which involved the use of conditions to an administrative approval in order to accomplish an object over which the Commission had no direct jurisdiction points in the same direction. Finally, it was not said by the Court that the decision of the Commission under review was within permissible limits of fairness and equity. This Court held merely that the Commission's decision was "a judgment that can justifiably be reached in terms of fairness and equitableness, to the end that the interests of the public, the investors and the consumers might be protected" (332 U. S. at 209).

This Court in the second *Chenery* case interpreted the Commission's order as making the findings necessary to support a self-executing "negative" order. The Commission did not make the findings in its opinion and order of February 7, 1945, which would present to this Court the question of the legal rights of petitioners in a "fair and equitable" reorganization under the Act. There is not a line in this Court's opinion which suggests that it was upholding an adjudication by the Commission of the legal rights of petitioners in a "fair and equitable" reorganization on the basis of its administrative experience. This Court held that the Commission had the power to establish a policy or pass a rule based upon its administrative experience. This rule was not retroactive. It took into consideration past events but not for the purpose of adjudicating

rights and liabilities but only for the purpose of establishing a new rule for the future prohibiting reorganization plans that treated stock purchased by officers or directors pending reorganization in the same way as other stock.

Because the Commission was not making an adjudication but was passing a rule, this Court held that the Commission's decision came within an area where Congress intended that the Commission's judgment was conclusive.

In *Securities and Exchange Commission* v. *Central-Illinois Securities Corp.*, 338 U. S. 96 (1949), the Court said (p. 127):

> "Administrative determinations of policy, often based upon undisputed basic facts, in an area in which Congress has given the agency authority to develop rules based upon its expert knowledge and experience, are exemplified by *Securities and Exchange Commission* v. *Chenery Corp., supra,* in which the Commission determined that preferred stock purchased by management in the over-the-counter market during the formulation of a holding company reorganization plan could not be exchanged for common stock participation in the reorganized company, as could other preferred stock; instead management was to be paid cost plus interest for the preferred stock so purchased.
>
> "The Commission's determination was made in the exercise of its duty to determine that a plan is 'fair and equitable' within the meaning of § 11(e) and that it is not 'detrimental to the public interest or the interest of investors or consumers' within the meaning of § 7(d)(6) and 7(e). On certiorari to the Court of Appeals which had reviewed the Commission's order under § 24(a) of the Act, we held that the Commission's action was 'an allowable judgment which we cannot disturb.' 332 U. S. 194, at

209. This holding was not based upon the fact that the Commission's order was reviewed under § 24(a) of the Act rather than under § 11(e), but upon the ground that the Commission's determination was made in an area in which Congress had delegated policy decisions of this sort to the Commission, and therefore that the agency determination was 'consistent with the authority granted by Congress.' *Id.* at 207. We think this view is applicable when review is had under § 11(e) as much as when it arises under § 24(a)."

On the other hand, the Court below said (Op. p. 7):

"But in the reorganization and merger proceedings the Commission was not laying down rules of conduct for the future in the exercise of its quasi-legislative power. On the contrary it was acting in a quasi-~~legislative~~ JUDICIAL or adjudicatory capacity to determine the existing obligations and duties of the holding companies in question and the rights of their creditors and stockholders under the legal standards laid down in the Act and in the light of their past conduct."

The conflict between the decision of this Court and the decision of the Court below is clear.

The entire superstructure of the opinion of the Court below is based upon the independent judgment of the Court below as to what the issues were in the second Chenery case. But the opinion of this Court controls the meaning of its mandate and the opinion of this Court shows that it was determining that it was within the power of the Commission to adopt a policy by the exercise of its administrative experience—not to make an adjudication of the legal rights of petitioners as of October 31, 1941, in the reorganization of Federal Water Service Corporation.

*In Prentis* v. *Atlantic Coast Line Company,* 211 U. S. 210, 226 (1908), this Court said:

> "* * * A judicial inquiry investigates, declares and enforces liabilities as they stand on present or past facts and under laws supposed already to exist. That is its purpose and end. Legislation on the other hand looks to the future and changes existing conditions by making a new rule to be applied thereafter to all or some part of those subject to its power.* * *"

Reference might also be made to *Arizona Grocery Co.* v. *Atchinson, T. & S. F. Ry.,* 284 U. S. 370 (1932), where this Court said (p. 389):

> "* * * The rule of estoppel by judgment obviously applies only to bodies exercising judicial functions; it is manifestly inapplicable to legislative action. * * *"

There is, it is submitted, no question of *res judicata* in this case. There was a rule which prevented Federal from treating the stock of petitioners in the same way as other stock was treated. This rule was in effect from February 7, 1945, to October 1, 1947, when the Commission interpreted the statutes so as to abrogate the rule. Since October 1, 1947, there has been no legal impediment to Federal's treating the stock of petitioners in the same way as other stock was treated.

**Second: If this Court affirmed an order of the Commission holding "fair and equitable" the second plan, the decision of this Court was not *res judicata,* but was binding on the lower courts only as the "law of the case."**

This Court in *Securities and Exchange Commission* v. *Central-Illinois Securities Corp.,* 338 U. S. 96 (1949), rec-

ognized that the same plan might come before a court both under Section 24(a) and under Section 11(e). This Court said (p. 123):

> "Conceivably the same plan might be brought under review by both routes. Indeed, in one instance the District Court for Delaware, to which the plan here was submitted, held that its determination of the issues in a § 11(e) proceeding was precluded by a prior affirmation of the same order by a Court of Appeals in a § 24(a) review proceeding. See *L. J. Marquis & Co.* v. *Securities & Exchange Commission*, 134 F. 2d 822, and *Application of Securities and Exchange Commission*, 50 F. Supp. 965. * * *"

In the case cited, *Application of Securities and Exchange Commission*, 50 F. Supp. 965 (D. Del. 1943), the Court did not consider itself bound by the order of affirmance, except with respect to the issues actually passed upon by the appellate court. The District Court considered the applicable principle to be "the law of the case." There was no suggestion that the principle of *res judicata* was applicable (p. 966).

It was recognized by this Court in *Insurance Group Committee* v. *Denver & Rio Grande Western R. R.*, 329 U. S. 607, 611 (1947), that, even after a plan of reorganization has been confirmed on review, the bankruptcy court might nevertheless take cognizance of subsequent changes in conditions and order the plan reexamined.

It is submitted that the appropriate legal doctrine to be applied to an affirmance of an order approving a plan of reorganization after review under Section 24(a) is the "law of the case", not *res judicata*. The decision of the appellate court is binding on an enforcing court with respect to the points actually passed upon but not as to the points

that might have been passed upon. See *Hartford Life Insurance Co.* v. *Blincoe,* 255 U. S. 129 (1921). And the decision of this Court while binding upon the lower courts is not binding upon this Court. *Messenger* v. *Anderson,* 225 U. S. 436 (1912).

**Third: The objections of petitioners to being deprived of their property where there is no rule could not be presented to this Court in the prior proceedings where the Commission claimed there was a rule. The present objections are therefore based upon new facts not available to petitioners in the prior proceedings and there is no estoppel by judgment.**

It is not easy to see the application of the doctrine of *res judicata* to a decision that is based upon administrative experience. Since the experience of the Commission is constantly changing and it is the policy of the law not to estop the Commission by judicial judgment, the issues arising today are always different from those arising yesterday.

We also know of no authority applying the doctrine of *res judicata* to an affirmance of a Commission order where the affirmance is not based upon the independent judgment of the Court as to the "case or controversy" involved.

But treating from the standpoint of *res judicata* the decision of the Commission as affirmed, the issue which was before the Court in the amendment to the merger agreement proceedings was whether petitioners were entitled to be treated on the same basis as other stockholders when such treatment was in conflict with a policy adopted by the Commission for the protection of the public. This is a different issue from the claim of petitioners to be treated on the same basis as other stockholders when such treatment is not in

opposition to any policy. There are numerous cases holding that the principle of estoppel by judgment does not apply to claims or demands which were not available at the time the first judgment was entered. See 2 Freeman on Judgments (5th ed. 1925) §§ 712, 713; 50 C. J. S. "Judgments" § 650, p. 92, and § 712b, p. 180. Petitioners had no opportunity to contest the validity of an order of the Commission determining that it was fair and equitable to penalize them with respect to their purchases and not penalize officers and directors of other companies who purchased securities while a plan of reorganization was on file with the Commission. They could not raise this objection to the deprivation of their property by the Commission until after the decision of this Court was made. Correspondingly, Federal was defeated by the Commission and the Court in its application to amend the merger agreement because of the existence of a policy. When this policy was abandoned a new claim or demand came into existence which had not been passed upon by the Court.

In *Utter* v. *Franklin*, 172 U. S. 416 (1899), there was a petition for a writ of mandamus to compel the defendants to issue certain bonds in exchange for bonds issued in aid of a railroad. This Court had held the bonds invalid in *Lewis* v. *Pima County*, 155 U. S. 54 (1894). There was, however, curative legislation and in the subsequent suit, it was held that mandamus should have issued. With respect to the doctrine of *res judicata*, the Court said (172 U. S. at 424):

> "* * * The judgment in that case was *res adjudicata* only of the issues then presented, of the facts as they then appeared, and of the legislation then existing."

Here, the Commission stated that it had a rule or policy and this was held to be within the power of the Commis-

sion. It subsequently abandoned the rule or policy and there would be now no legal obstacle to another application for leave to amend the merger agreement. Federal, in justice to other stockholders, could not postpone its liquidation in order to present another plan (3a) before filing plan 4. But this would not affect the legal rights of petitioners.

**Fourth: Federal Water and Gas Corporation is the same corporation as Federal Water Service Corporation.**

Counsel for the stockholders protective committee made the point before the Court below that Federal Water and Gas Corporation was a separate corporation from Federal Water Service Corporation. Unfortunately the Court adopted the contention. The fact is that the merger was a true merger in which one corporation continues its existence. It was not a consolidation. Utility Operators Company and Federal Water and Gas Corporation were merged into Federal Water Service Corporation which continued its corporate existence, became the surviving company and adopted the name of Federal Water and Gas Corporation under the laws of Delaware. The facts are correctly stated by the Securities and Exchange Commission in the first opinion, 8 S. E. C. 893, 898 (1941). Paragraph Fourth(d) of the merger agreement should be looked upon as an amendment to the corporate charter of Federal Water Service Corporation.

This point is unimportant because if the rights of petitioners are to be judged in accordance with legal principles, it would make no difference what corporate machinery was used in order to "freeze out" them from their interest in the assets of Federal—whether by merger, *Outwater* v. *Public Service Corporation of New Jersey*, 103 N. J. Eq. 461, 143 Atl. 729 (Ch. 1928); consolidation, *Jones*

v. *Missouri-Edison Electric Co.*, 144 Fed. 765 (8th Cir. 1906); or sale of assets, *Southern Pacific Company* v. *Bogert*, 250 U. S. 483 (1919); *Geddes* v. *Anaconda Copper Mining Company*, 254 U. S. 590 (1921); *Ervin* v. *Oregon Ry. & Nav. Co.*, 20 Fed. 577 (C. C. S. D. N. Y. 1884); *Nave-McCord Mercantile Co.* v. *Ranney*, 29 F. (2d) 383 (8th Cir. 1928). Even where there was no "freeze out" but an amendment to a corporation charter was in violation of the vested rights of preferred stockholders, the preferred stock was treated as outstanding and not destroyed by the void amendment. *Keller* v. *Wilson & Co., Inc.*, 21 Del. Ch. 391, 190 Atl. 115 (Sup. Ct. 1936).

Petitioners, of course, have had no rights under the merger agreement since October 31, 1941, except to surrender their stock and receive $313,190.22. They have contended, however, that the merger agreement was invalid with respect to their stock and was not effective to deprive them of their vested rights of property in the assets of Federal. This contention cannot be answered by saying that the Commission prevented petitioners from becoming stockholders in Federal Water and Gas Corporation. Petitioners bought an interest in Federal Water and Gas Corporation and the question is whether the order of the Commission was effective to deprive them of it.

## CONCLUSION

From a technical standpoint, it is submitted that the Court of Appeals has decided a federal question in a way probably in conflict with the applicable decision of this Court. The federal question is with respect to the jurisdiction of the Commission over the stock of officers and directors and controlling stockholders, which was purchased by them while a plan of reorganization was on file with

the Commission. The Court below has held that the Commission has jurisdiction to adjudicate on the facts in a particular case that, in a fair and equitable plan of reorganization, such officers and directors have no claims against the corporation except to recover cost. The decision of this Court, which is supposed to be the basis for this decision, goes no further than to hold that the Commission has power to deny an application by a corporation for approval of a reorganization plan or an amendment to the plan which treats such stock in the same way as other stock is treated, provided the denial is in pursuance of a rule or policy having applicability to purchases of stock by officers and directors of holding companies generally. The decision of this Court is based upon the power of the Commission to develop rules and the decision of the Court below rests upon the asserted power of the Commission to make an adjudication.

Apart from the technical aspects of the application for the writ, it is submitted that when this Court once takes a case on certiorari and a question arises in a subsequent proceeding as to the interpretation of its mandate, this Court should take the subsequent case on certiorari in order that its mandate shall be correctly interpreted and applied.

Respectfully submitted,

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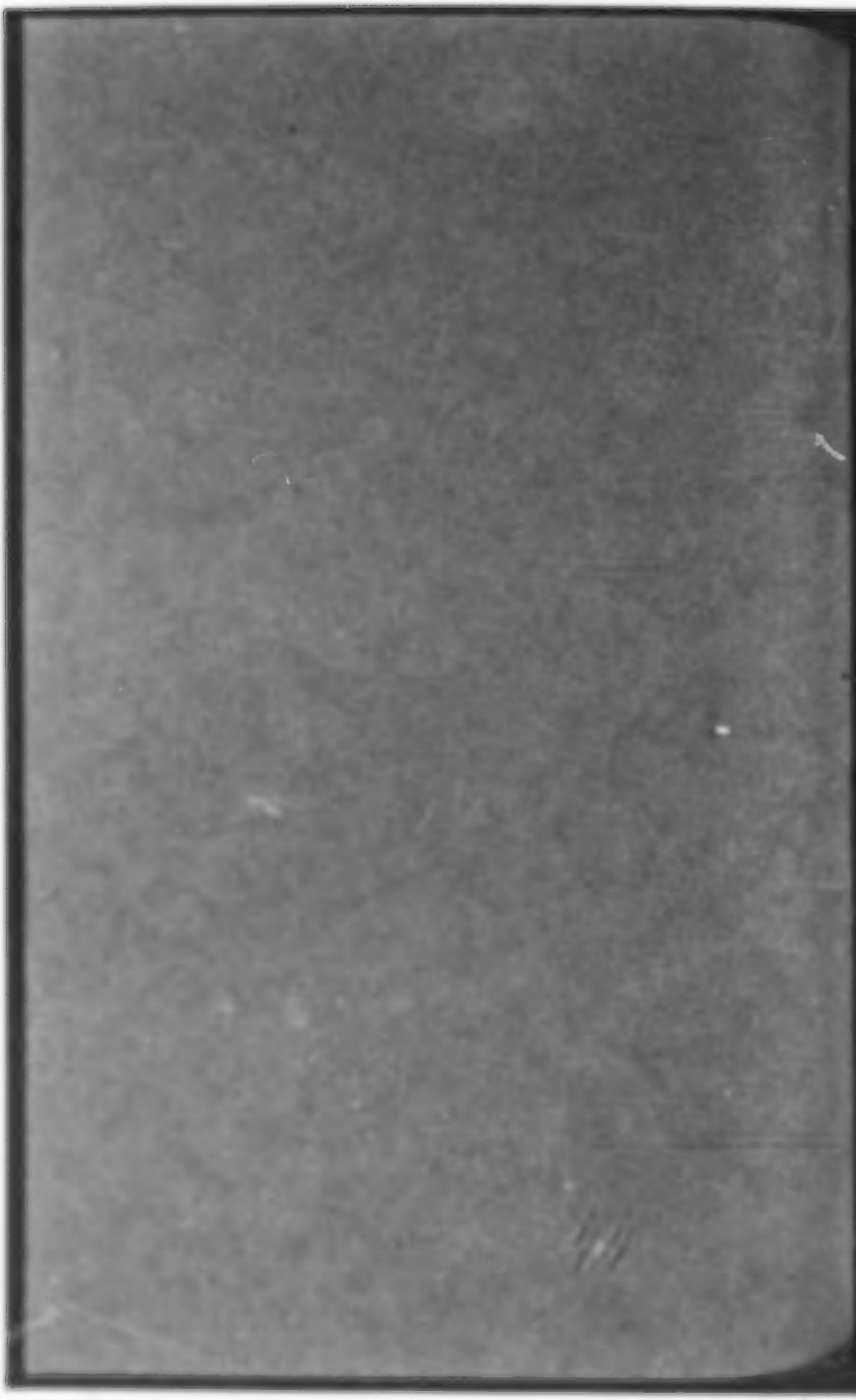
Dated, May 17, 1951.

[redacted]



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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1950

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No. 709

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CHENERY CORPORATION, et al.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION, et al.

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## MEMORANDUM ON BEHALF OF FEDERAL WATER AND GAS CORPORATION COMMON STOCKHOLDERS' COMMITTEE, RESPONDENT

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### Preliminary Statement

This brief is submitted by respondent, Federal Water and Gas Corporation Common Stockholders' Committee, for the purpose of demonstrating that the petition of Chenery Corporation, et al., for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit should be denied.

### Opinions Below

The opinion of the Court of Appeals (R. 317-326) is not yet reported. The opinion of the District Court (R. 52-58) is reported in 87 F. Supp. 289. The opinions and orders of the Securities and Exchange Commission (R. 7-32; R. 34-38), dated July 2, 1948, and July 27, 1948, not yet officially reported, are contained in Holding Company Act Releases Nos. 8313 and 8387.

## Jurisdiction

The jurisdiction of this Court is invoked under U. S. Code Title 28, Section 1254(1).

## Questions Presented

(1) Whether petitioners may collaterally attack the final decree of the Court of Appeals for the District of Columbia, entered pursuant to the mandate of this Court in *Securities and Exchange Commission* v. *Chenery Corporation,* 332 U. S. 193, affirming the order of the Securities and Exchange Commission issued February 7, 1945.

(2) Is a plan under Section 11(e) of the Public Utility Holding Company Act of 1935 that provides for prior payment in full and in cash of creditors' claims fair and equitable as to them?

## Statement

This respondent appears on behalf of the public holders of the outstanding 976,303 shares of common, the only class of stock of Federal Water and Gas Corporation outstanding. This is the stock that was issued to those, other than petitioners Chenery Corporation and others (Chenery et al.), who formerly held the preferred stock of Federal Water Service Corporation, pursuant to a plan filed by the latter corporation under Section 7 of the Public Utility Holding Company Act (Act) for its reorganization by merger with Federal Water and Gas Corporation and Utility Operators Company. That plan was amended to provide that in lieu of receiving new stock of the corporation resulting from the merger (new Federal Water and Gas Corporation), Chenery et al. should have only a claim against that corporation for the cost of their old Federal Water Service Corporation preferred stock, with interest

to October 31, 1941 (the effective date of the merger plan), a total of $313,190. The merger plan was approved by order of the Securities and Exchange Commission (Commission) on September 24, 1941. That order having been set aside by this Court and the case remanded to the Commission for further proceedings,[1] the Commission entered an order on February 7, 1945, reapproving, as of September 24, 1941, the amended reorganization plan.[2] Finally, pursuant to a mandate of this Court upon a second appeal by Chenery et al.,[3] the Court of Appeals for the District of Columbia on December 12, 1947, entered an order affirming the Commission's order of February 7, 1945 (R. 65).

The stockholders represented by this respondent constitute (1) those who in the merger proceedings consented to the merger upon the petitioners' express agreement (which, by these proceedings, the petitioners continue to violate) that, in the event it should be "finally determined that said order . . . shall be affirmed", they, the petitioners, would surrender their stock for cost plus interest, as provided in the merger agreement (R. 13, fn. 6); and (2) those who subsequently bought their stock in the public market from such original recipients in reliance upon the orders of the Commission, affirmed by this Court (332 U. S. 194), which adjudged petitioners to be creditors, not stockholders, of Federal Water and Gas Corporation.

In consequence, the present common shareholders of Federal Water and Gas Corporation, represented by this respondent in these dissolution proceedings, are the equitable owners of and entitled to receive the assets of their corporation, subject only to the prior payment to peti-

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[1] *Securities and Exchange Commission* v. *Chenery Corporation et al.*, 318 U. S. 80 (1943).

[2] *Federal Water Service Corporation*, Holding Company Act Release No. 5584.

[3] *Securities and Exchange Commission* v. *Chenery Corporation et al.*, 332 U. S. 194 (1947), rehearing denied, 332 U. S. 783 (1947).

tioners (creditors who are not and never have been stockholders of their corporation) of the sum of $313,190, heretofore adjudged to be due petitioners in consequence of their having been preferred stockholders of the old and now defunct merged Federal Water Service Corporation.

## ARGUMENT

(1) Petitioners urge that the question presented by their present application is whether the Court below gave proper effect to the decisions of this Court in the first and second Chenery cases. In reality, however, the question presented is whether the Court below gave proper effect to the *mandate* of this Court in the second Chenery case by refusing to permit a collateral attack by petitioners upon that mandate, which adjudicated them creditors of Federal Water and Gas Corporation in the sum of $313,190. Recognition of this distinction exposes the basic fallacy in petitioners' presentation. The opinion of this Court, as it articulates the reasons for its ultimate determination or states principles of general application, is of importance when it is to be used as a basis for a like result in a case involving different parties or other facts. But here the important factor is not the reason for this Court's prior adjudication but rather the adjudication itself.

By the mandate as followed by the Court of Appeals for the District of Columbia, this Court has adjudicated that petitioners are entitled only to claim against the assets of Federal Water and Gas Corporation as creditors and not as stockholders. The Court below in holding that petitioners could not collaterally attack the adjudication of their creditor status and that a plan that provided for payment in full of their creditor claim was fair and equitable determined nothing new or novel—determined nothing of which this Court should take jurisdiction.

The opinion of the Court below (R. 317-326) contains an able and conclusive answer to petitioners' efforts to avoid

the impenetrable bar of res judicata in this collateral attempt by them to relitigate their claim previously adjudicated. Rather than here documenting the reasons why that effort must fail, for brevity we respectfully refer this Court to the opinion written by Judge Maris for the Court of Appeals (R. 317-326).

(2) But even if the prior adjudication were not a conclusive bar, the equities of the situation require the conclusion that the status of petitioners as previously determined should not presently be disturbed. Petitioners are here attempting to invade property rights of the Federal Water and Gas Corporation stockholders as the sole owners of the equity in that Corporation. These rights were acquired: (a) as the result of approval of the merger by cestuis stockholders in reliance upon the commitment of petitioners (R. 13, fn. 6), their officers and directors, to deliver up their preferred stock holdings in old Federal Water Service Corporation for cancellation and accept a creditor claim status in the new Federal Water and Gas Corporation as awarded them by the Commission's order of September 24, 1941, approving the merger (R. 111), conditioned only upon it being finally determined that the Commission's order should be affirmed—as it was; and (b) by acquisition in the public market as innocent purchasers for value and in reliance upon the prior adjudication of the Commission, affirmed by this Court, of the stock issued in consequence of the merger approved by the prior stockholders in reliance upon petitioner's commitment, as last stated.

Attempting to disregard rules of res judicata, petitioners appealed below to the sound discretion of the Commission to reopen the old and completed merger proceeding and reconsider the equities which petitioners claim attached to their acquisition, while officers and directors of the defunct merged Federal Water Service Corporation, of its preferred stock; equities, petitioners contended, that should have moved the Commission and should now move this

Court to grant petitioners parity with other former preferred stockholders of Federal Water Service Corporation in the award of common stock of the present merged corporation under the merger plan (though the latter expressly provided otherwise) and to revoke the previous adjudications that gave petitioners a creditor and denied them a stockholder status in the present corporation.

But, absent any other consideration, the estoppel that flows from action taken in reliance upon this record bars such a plea. Petitioners agreed to be bound by an affirmance of the Commission's order; they expressly so represented to their former fellow Federal Water Service preferred stockholders in an effort to, and did thereby, induce them to vote for and cause the adoption of the plan of merger; petitioners expressly, as part of such representation and inducement, agreed, in the event of affirmance, to deliver up their stock for the $313,190 that has since been awaiting them; the condition for such delivery and cancellation of their old Federal Water Service stock occurred and has been an undisturbed and undisturbable fact since December 12, 1947; and these respondent stockholders, having relied thereon, petitioners are estopped from making claim upon their defunct certificates—pieces of paper which have no validity except as objects for cancellation concurrently with petitioners' acceptance and receipt of the $313,190 they agreed to and have consistently refused to accept.

Another simple equitable maxim must defeat this claim, were the doctrine of res judicata not an absolute bar—the maxim that equity regards that as done which ought to be done. Petitioners' present appeal to equity—could it be entertained—must meet the bar that petitioners are not and never have been holders of stock of the present merged Federal Water and Gas Corporation, that they were adjudged creditors thereof, that when their $313,190 was tendered to them, that money became (and is now) theirs and the stock certificates they held became (and

are now) nugatory. Had petitioners surrendered, for purpose of record cancellation, their otherwise worthless Federal Water Service preferred stock certificates, and accepted the $313,190 which was and has been held available to them, they would not now be in a position to present their present contention. And that is the very thing they expressly undertook to do, and the fact that instead, they violated their undertaking and withheld surrendering their stock certificates can give them no greater rights in equity than they would have had, had they faithfully abided by their commitment.

## CONCLUSION

WHEREFORE, for the reasons stated, i.e., first, because of the equitable bar of the principle of res judicata, and, second, by reason of the principles of estoppel, respondent submits that this Court should deny petitioners' application for a writ of certiorari.

PERCIVAL E. JACKSON,
Counsel for Respondent Federal Water and Gas Corporation Common Stockholders' Committee.